RICHARD RUSSELL'S DOW THEORY LETTERS, INC.
P. O. Box 1759, La Jolla, California 92038
Minimum of 26 Letters per year – $185 Annually
Registered with the Securities and Exchange Commission

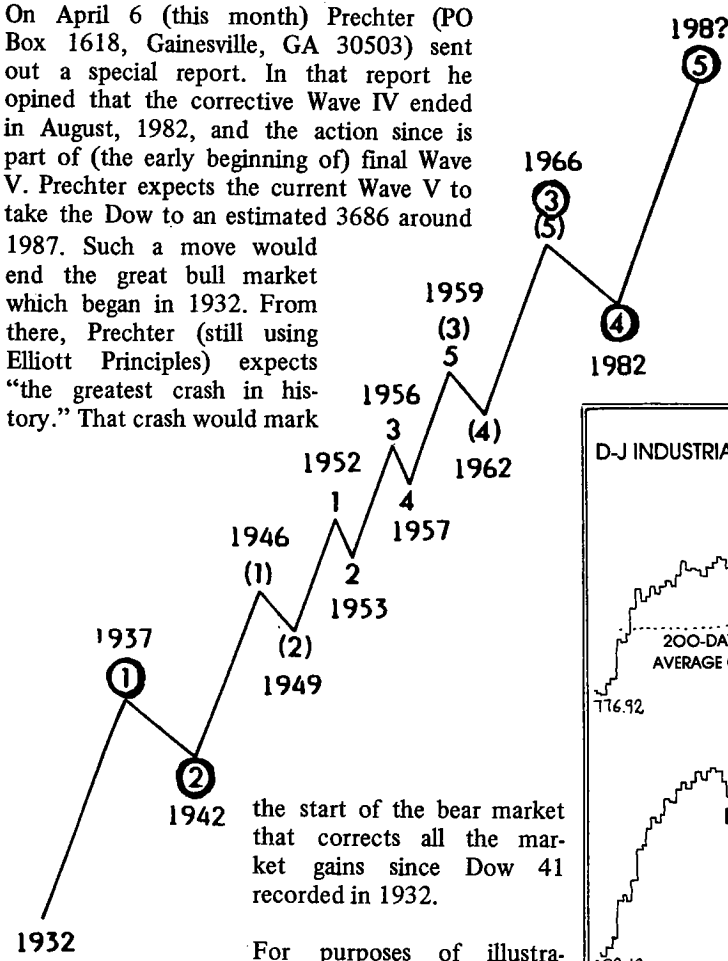
April 20, 1983 **LETTER 859**

April 8 DJIA 1124.71; PTI 1541; A-D Ratio –15.87
April 15 DJIA 1171.25; PTI 1575; A-D Ratio –14.71

THEORY: About six years ago I met with A.J. Frost, unquestionably the leading student of the Elliott Wave Principle at the time. Frost and I were going to write a book on the Wave Principle, the book partly to be based on a "coming, giant Fifth Wave conclusion" to the ongoing bull market. I begged off the project because I lacked the time. Instead, I suggested that Bob Prechter do the book with Frost (actually, I felt that Prechter was a much more dedicated and competent student of the Wave Principle than I was).

Their book, The Elliott Wave Principle, was published in 1978. The book advanced the thesis that somewhere ahead we could expect a giant Fifth Wave, the wave that would wind up the great bull market that began for the Dow on July 8, 1932 at 41.22.

On April 6 (this month) Prechter (PO Box 1618, Gainesville, GA 30503) sent out a special report. In that report he opined that the corrective Wave IV ended in August, 1982, and the action since is part of (the early beginning of) final Wave V. Prechter expects the current Wave V to take the Dow to an estimated 3686 around 1987. Such a move would end the great bull market which began in 1932. From there, Prechter (still using Elliott Principles) expects "the greatest crash in history." That crash would mark the start of the bear market that corrects all the market gains since Dow 41 recorded in 1932.



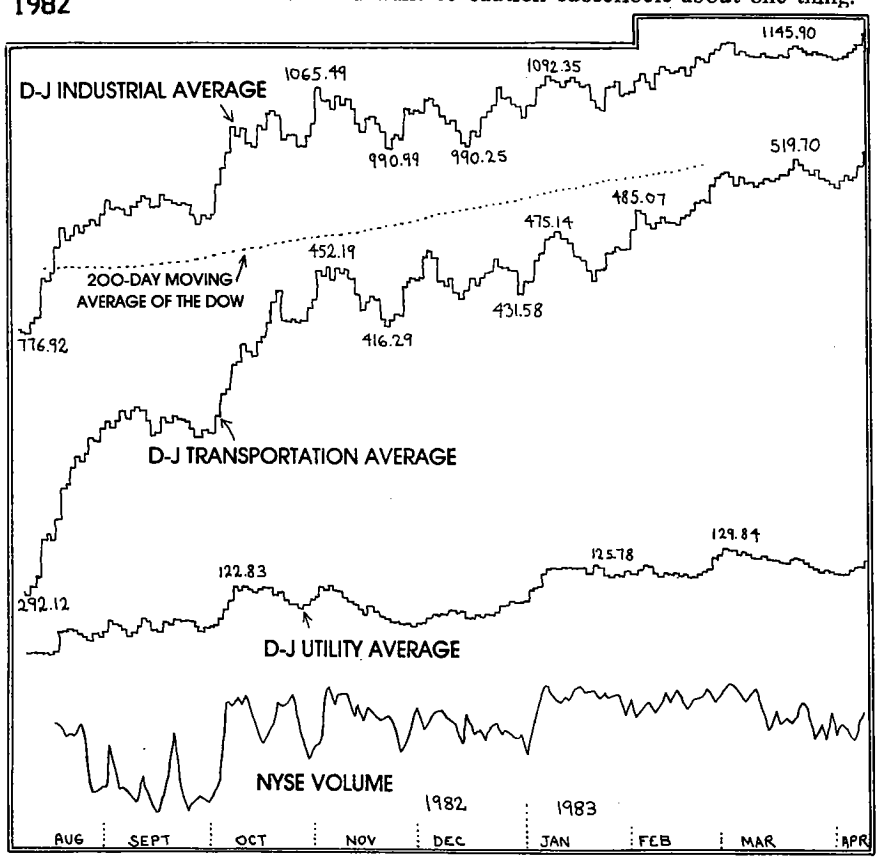
For purposes of illustration, I am including a Dow chart from Prechter's latest report. On this chart you can see how Bob delineates the various waves starting from the 1932 low. Wave 3 (1942 to 1966) "extended" twice, which means it sub-divided twice, based on the tremendous upward thrust following the 1942 low.

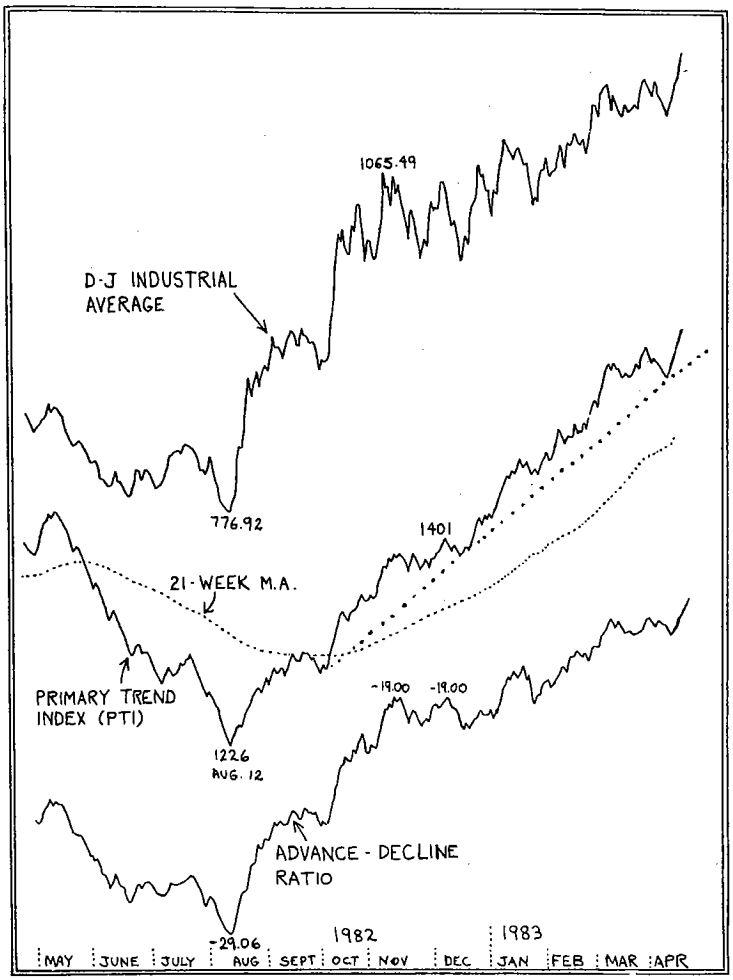
Why am I writing about this now? Well, for one thing I have followed Prechter's career since he started. And I was there with A.J. Frost when we puzzled over this whole Elliott possibility. And I know that this "final Fifth Wave" concept is something that the three of us have been kicking around (Prechter and Frost fully expected it) for years. And, finally, I am writing about this because the Dow, for the first time in history, has established itself *decisively* above 1100.

Back in 1977-78 Prechter, Frost and I expected the Fifth Wave to start within a year or so. What threw us off was *how long it took* for the Dow to make its move. As the years dragged on, I became skeptical. But Prechter and Frost stayed with their original Fifth Wave thesis. And now I'm wondering, is this finally, actually the beginning of the great Fifth Wave? Time will tell. But the possibility is there.

All right, let's get back to cold reality. By April 12, following the extended and tedious consolidation, just about everything on Wall Street broke out to new highs. The S & P 500 Composite was at a record high as was the NYSE Composite. The Dow recorded a new record high. The PTI surged to 1555, a new record high, and the A-D Ratio (for the NYSE) which had been lagging joined the parade to new highs.

As I said in the last Letter, this is a powerful bull market, no mistake about it. So far, the market has produced that relentless, grinding, "clawing-up" action so typical of true primary bull moves. But I want to caution subscribers about one thing.





A bull market needs plenty of leeway as far as the technical picture is concerned. I note that most analysts are watching this market with a magnifying glass. That's not going to work. For if this is indeed the start of the big Fifth (Elliott) Wave, we are going to see much strange and exotic action coming out of Wall Street.

The market is going to appear ragged for long stretches of time. Periods when the market "should" correct are going to become periods of sideways consolidation instead. The sentiment indicators are going to appear too bullish (which is normally bearish), but in a big bull market the crowd can be optimistic (and correct) for long stretches of time! We are going to see all kinds of divergences, "poor action" and red alerts. And all these will be calculated to keep people out of the market and in a state of high anxiety. But the bull will keep climbing. He won't be stopped by the usual items.

INVESTMENT POSITION: The bull remains in this box. As it has all along, the PTI continues to tell the story. And the story is bullish. Hold all your no-load

funds, hold your defense portfolio, and hold a solid, "safety and income" position in Treasury bills. All new money should go into the no-load funds. This is a "buy and hold" market, and over and over again those who have sold out on the hopes of scalping trading profits merely find that they are left behind. That's how a big bull market works. Leave it, and it leaves you behind. It's very, very hard to out-trade the primary trend when it's as solidly up as it is now.

QUESTION: Russell, go over again what you see coming up in the economy and the markets.

Answer: That's a tall order, and my current opinions are subject to revisions, but here's what I see at this time. I see a long "unwinding period" for the US economy. I term this an unwinding period because I feel we are now in the era of managing, re-scheduling, revamping, re-thinking the debt. The giant debt of the US, as it now stands, is almost unmanageable. If it continues to grow at the same rate as in recent years the debt could become totally unmanageable. But, as I see it, we are moving into a period wherein the debt problem will have to be faced. There will be all sorts of "treatments" for the debt, but basically this will be an unwinding period. And the KEY to the situation will be REAL INTEREST RATES.

When an investor can get a good, safe REAL return on his money, it is always tempting–and it is always competition for all other forms of investment. Right now the real return on T-bonds is about 6%, a very high figure (the real return, of course, is the actual bond return minus the current rate of inflation).

My feeling is that the real return on money will probably stay high over the foreseeable future. This would be a negative for gold, and I think it will tend to keep gold holding within a trading range. The high real return on money will also tend to keep investors out of collectibles, it will make buying a house simply an exercise in finding a place to live (rather than as an investment). And the high real return will tend to inhibit inflation, thereby producing an atmosphere that the stock market likes.

I continue to feel that the stock market is the most interesting place to be, and I feel that this will continue for quite a while, maybe a matter of years. Consequently, I think the stock market is now a "buy and hold" market, something we haven't seen in many years.

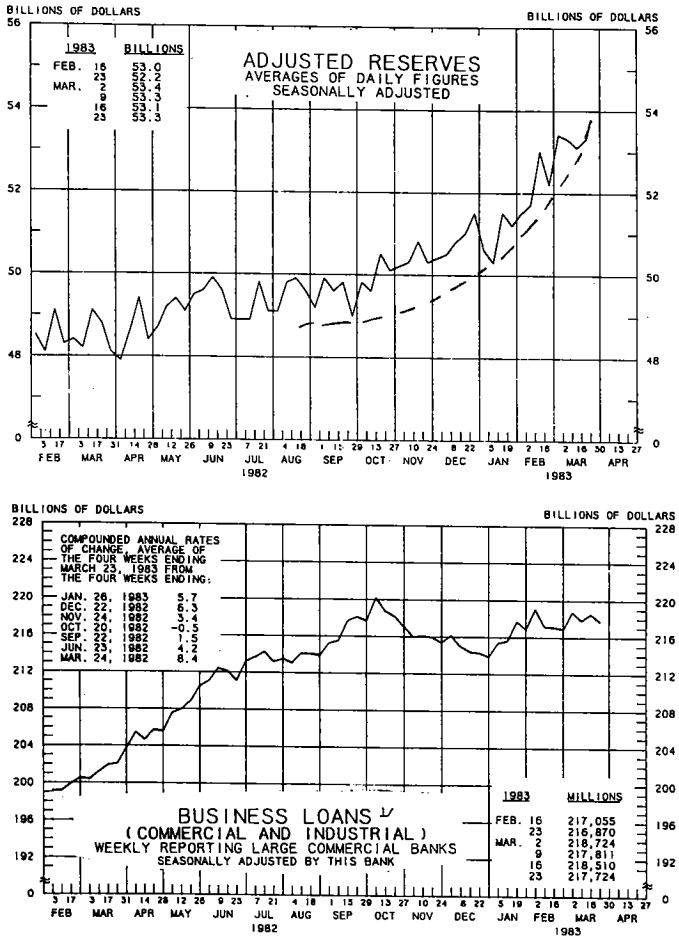
As for the economy, we are looking at an economy in a state of "high-flux." The changes coming up in the American economy will be massive. We are losing out in the production of many smokestack items with the greatest example being steel. On the technology front, the US will be in a continual international competition for the newest and best products, and fortunately the US mind is very inventive when the need arrives. And believe me, the need has arrived.

The US's absolutely dominant position in high-technology has ended, and many other nations (particularly Japan) are now leading in some areas and closing in in other areas. In many segments of consumer electronics(VHS recorders, TV sets, Hi-Fi equipment) the Japanese have literally taken over the markets. It's up to US manufacturers to develop new concepts, new items and new uses–before its international competitors do.

Question: I notice that the talk about a banking collapse and illiquidity at the banks has now died down. In fact, it has almost disappeared. What's happened?

Answer: The answer can be easily illustrated with two charts. The first shows the adjusted reserves in the Federal Reserve system. Since last September these reserves have been going up at an exponential rate. For instance, for the four weeks ending March 23 the compound annual increase was 34.9%. This is an incredible rate, and it means that the banks are flooded with liquidity.

How about borrowing at the banks? This chart shows that business loans from the reporting banks have been flat ever since the peak recorded last October. Thus with reserves building and loans flat, the banks are now in a state of building liquidity.



Question: Russell, you have been writing about a gigantic US defense build-up, but I note that Congress is really fighting the build-up. What do you see happening in this area?

Answer: I have been stating that Russia is moving towards undisputed military superiority. Already, Russia is intimidating Europe with its SS-20s plus KGB terrorism. The Vietnamese have launched a new offensive in Cambodia and that involves a US ally, Thailand. The Russians are assuming increasing power in strategic spots like the Red Sea. And through Cuba, the Russians are sending out carloads of military equipment to sundry Soviet military enterprises in the Caribbean. Obviously, additional tons of Soviet equipment are going into Central America.

But I continue to believe that the "shock of recognition" is coming. That shock will be a major Russian takeover (possibly in the MidEast), and it will be seen that the US does not have the military ability to halt or reverse the situation. Then there will be a panic to "catch up" to the Russians.

In my opinion, the Russians fully believe that time is on their side. Every month, every year that goes by now favors the Russian military position. We talk, we dawdle, we argue, we compromise, we investigate–and the Russians build.

But what about agreements? And I say again, the Russians aren't interested in military agreements (unless such agreements favor the Russians). The Russians are interested in ultimate victory. They have a goal. We simply react. By the way, this piece from the April 11 WSJ editorial should give you some idea of whether Russia is pulling back on its plans for world domination.

We don't want to exaggerate. We know as well as anyone that there are no Soviet armored divisions on the Mexican and Canadian borders. And although Havana is a mere 75 miles from Key West, Cuba harbors only 11,500 Soviets, 200-plus MiGs, an arsenal of naval cruise missiles, SAMs and Apex and Aphid air-to-air missiles, several dozen large troop transport planes and a fleet of frigates, torpedo boats and attack submarines. There is no point in being alarmist over the fact that in 1981 and 1982, the Soviets delivered 132,000 tons of arms to the island, the highest level of shipments since the Cuban missile crisis in 1962.

Elsewhere in the Caribbean basin, Cubans are building a high-performance jet staging airfield in Grenada, near the Atlantic shipping lanes. Bulgarians have hauled Nicaraguans off to Europe to teach them to fly MiGs, East Germans are instructing Nicas in secret police tactics, Cubans are indoctrinating their teen-age youth in how to hate and someday kill Yankees, and Russians are directing the Sandinista communists in the fine art of consolidating political control. Nicaragua is the support base for guerrillas seeking to overthrow the governments of El Salvador, Guatemala, Honduras and Colombia. All this is given a heroic revolutionary gloss by front groups operating with free speech protections in the U.S. A murderous military government has just taken over Suriname and turned its eyes to Cuba. And then there's that quiet little Soviet base, ostensibly a Lada car distributorship, in the Panama Canal Free Zone, a few hundred yards from the Atlantic-side Gatun locks and about the same distance from a top-secret U.S. naval communications facility.

Elsewhere in Latin America, 150 Soviet military advisers still are in Peru, working closely with the Peruvian military even though Peruvians elected an anti-communist civilian government three years ago. Argentina, which may soon call on the Peronists for another deadly dose of populism-fascism-socialism, has become highly dependent on the Soviets as a market for grain and foodstuffs. Bolivia's new civilian president has communists in his government and flirts with Castro.

BOOKS AND THE PATH: Each year approximately 400,000 manuscripts are submitted to publishers in the US. Of these, roughly 40,000 are published, an incredible amount. Last night I sat down and thought about how a few books have changed my life. When I was about 18 years of age I spent a summer reading all of the works of the great Russian novelist, Dostoievski. His powerful novels made a lasting impression on me. Dostoievski was an intuitive genius, a pathological gambler, and a prodigious writer. No fiction that I have ever read before or since has affected me as much as the writing of Dostoievski. Freud, who corresponded with Dostoievski, once wrote of him, "Intuitively, Dostoievski knew everything that I discovered."

Then in the early 1950s I discovered the writing of Robert Rhea. I don't know how or why, but the New York Public Library had a complete set of Rhea's reports (written 1932 to 1939). I had spent the previous 6-8 years trying to make sense out of the stock market (actually, I worked at this ever since I graduated from college in 1945). I liked Garfield Drew's odd lot studies and his technical studies, and I liked some of Schabacker and, of course, Edwards & Magee. But when I sat down to read Robert Rhea, that was a real revelation. I knew that I was reading the work of a genuine genius. And for the first time, many of my questions and thoughts about the stock market were answered.

I read and re-read Rhea (who died in 1939) for two solid years. I followed his thinking letter by letter. I was so steeped in Rhea

that for a while I think I lost my mind and began to believe that I was his reincarnation. I mean I got so I thought I could write his reports. And of course, eventually, based on what this man (dead for 15 years) had taught me, I did write my own Letters. But my debt to Rhea was inestimable. He was my stock market godfather.

I moved to California in 1961. I was in ferment, society was in ferment, and the "beats" had given way to the "hippies." I had gone to high school with Jack Karouac in NYC, and I had read most of his books. They made a big impression on me, particularly his famous novel, "On the Road." But when I got to California I discovered that I had other problems, and they were basically problems with the way I saw myself, the way I saw the world, and the way I saw myself in relation to the world. I guess it was around 1970 that I came upon a book that again changed my life. The book was by Dr. Frederick S. Perls and the book was entitled "Gestalt Therapy Verbatim." I had already spent four years in classical Freudian analysis. That was back in 1950-55. But I found that analyzing and analyzing and more analyzing didn't get me anywhere. I kept waiting for me to change. I kept waiting for my world to change. Nothing changed–at least not that much.

But that book by Perls, it set me on my ear. I couldn't put it down. I must have read the first 60 pages of that book 500 times. Perls had a new and different way of percieving the human condition. To put it mildly, it was another revelation for me. Here, I'll give you a bit of Perls from the introduction to his book. He states:

"Now the problem. . . . is with the whole American culture. We have made a 180-degree turn from puritanism and moralism to hedonism. Suddenly, everything has to be fun, pleasure, and any sincere involvement, any real *being here,* is discouraged."

Then Perls, who fancied himself a bit of a poet, inserts this poem:

"A thousand plastic flowers
Don't make a desert bloom,
A thousand empty faces
Don't fill an empty room."

Perls taught me to stop being a phoney–to myself and to others. He taught me (and I'm still working on this one) that the most important gift you can receive in this world is the gift of yourself. If you don't have yourself you can have all the money in the US Treasury–and you're nothing. If you do have yourself you will find that what you need will come to you. What is the way to the self? I'll tell you the secret in three words: commitment, searching, pain. And that, I suppose, is why so few people make the world's most important journey.

NOTES & QUOTES: The amount of money large corporations spend on legal fees is absolutely mind-blowing. This list from the NY Times gives you some idea of the expenses involved. Do you believe it–AT & T has almost one thousand in-house lawyers!

Largest Corporate Legal Staffs

In-house legal departments ranked by number of lawyers in 1982

	1982	1981
A.T.&T.	914	895
Exxon	447	454
General Electric	318	340
Mobil Corp.	232	232
Standard Oil (Ind.)	211	209
Prudential	202	204
Sears Roebuck	201	146
Ford	186	192
Du Pont	182	180
Atlantic Richfield	164	169
Gulf Oil	152	145
I.B.M.	146	141
Tenneco	145	135
BankAmerica	132	158
General Motors	125	125

Source: 1983-84 Directory of Corporate Counsel

* *

The Wall Street Journal continues to put out the most intelligent and courageous editorials in the business (at least in my opinion). On April 6 the Journal published a particularly brilliant editorial entitled, "It's Sellout Time Again." I couldn't resist including this section of that editorial (and I would urge all my subscribers to read the WSJ editorials).

Let's review the budgetary history of the Reagan administration and Congress these last two years. When Ronald Reagan came into office he took a knife to the 12% fiscal '82 spending increase planned by Jimmy Carter and carved away $44 billion. But by the time the fiscal year had ended last Sept. 30, $33 billion of that had grown back. Federal spending as a share of GNP reached a new post-World War II high.

The current fiscal year has been even worse. Just over a year ago, the president projected fiscal '83 spending that would have been up only 6% from fiscal '82. Currently, the projected increase is 11%. And all this is happening at a time when inflation has fallen below 5%. If the present ratio between the federal budget and national economic growth should continue for another decade, Washington's share of gross national product would rise to 50% from 25%. And that is optimistic in that it assumes that GNP growth would not be stalled at some point, as it has been in various other countries, by continued expansion of welfare state production disincentives. As we have argued in the past, the U.S. economy already shows signs of this disease.

Congress, however, is not content with our current level of hazard. Just before vacation last month, the House raised this year's Reagan ante by nearly $10 billion and tacked another $15 billion onto what the White House was proposing for next fiscal year, proposing to finance this latest self-indulgence with $30 billion in new taxes. The most convenient way of obtaining these new revenues would be repeal of this year's scheduled tax rate cut and the 1985 indexing of tax rates that was designed to end the insidious erosion of take-home pay through bracket creep. Tip O'Neill and Co. believed they had received a thought message last November saying "tax, tax, spend, spend." Four House Republicans, Schneider of Rhode Island, Green of New York, Jeffords of Vermont and Rinaldo of New Jersey, joined in their hymn to the glorious stagflationary past.

ANNOUNCEMENT: A few months ago I spoke in San Diego (an E.F. Hutton sponsored event) with Hutton's chief gold analyst, David Hillson. Hutton planned for 400, and we ended up with 800 attendees. The Hutton people in Beverly Hills have now asked me to speak, and I have agreed. I'll be appearing again with Mr. Hillson, this time on April 27 at the Century Plaza. The price is right–$10 for a single and $15 for a couple. As before, Hutton has informed me that I can say what I want, the way I want, and it all starts at 7:30 P.M. The subject again is basically gold, but I'll be talking about a lot of items, and there will be a question and answer period.

From our "Signs of the Times" Dept: If Reagan does not run, there is hushed talk of George Bush for President and Sandra Day O'Conner for VP on the Republican ticket. For the Dems there is talk of Mondale for President and a black (maybe LA Mayor Bradley) for VP. But the odds look increasingly as though Reagan will go for it.

* *

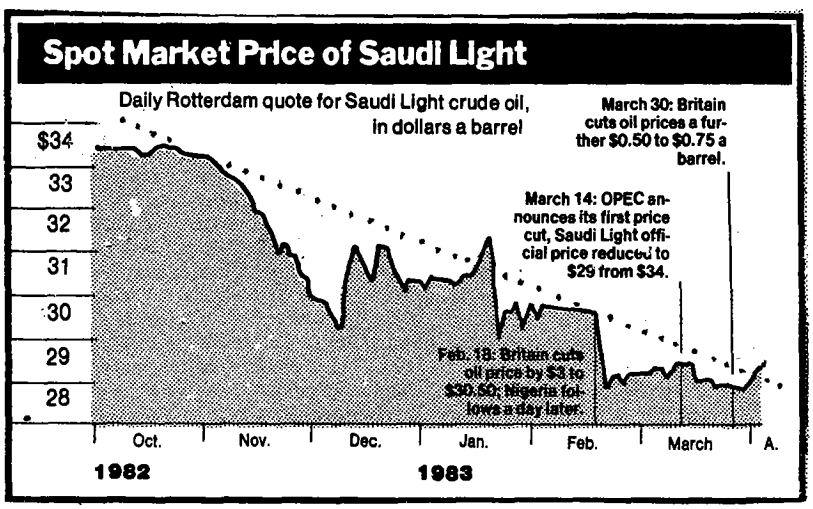
In a recent article, Lawrence K. Roos (retired head of the St. Louis Federal Reserve Bank) questions what is going on with the money-supply explosion.

> **Whether our monetary policy makers have the resolve to exercise the monetary discipline that brought inflation and interest rates from double-digit levels to where they are now remains to be seen. The political pressures for continued ease, especially in an election year, will be intense. Unless the Fed, in its proper role as an independent central bank, reverts to an anti-inflationary course, we will soon be faced with a resurgence of inflation, resultant higher interest rates, a weaker economy and severe disincentives for capital formation.**

* *

"The whole world is bearish on oil." Everybody knows that oil is about to "plunge to the lower depths." Everybody, except those buying the oil stocks and those actually buying oil. The whole oil complex including the domestics, the internationals and even the oil equipment makers (I'm talking about the stocks) hit their lows last August. And they haven't been lower since. Personally, I think the oils have bottomed out, and I think the higher yielding international oils (Exxon, Texaco) are a buy (they yield 9% so you can buy them like bonds).

This chart (from NY Times) shows the spot price of Saudi light (crude) since late last year. Actually, the price of crude is ABOVE its price of a year ago although this doesn't show on the chart. I've drawn a trendline, and it does seem as if an upside reversal is here. The new crude oil commodity contract (the contract is only a few weeks old) is hitting highs. Maybe what everybody knows isn't happening!



Some of the defense stocks on our list are starting to do pretty well. BDM International has made a big move. Last week LFE and Planning and Research hit new highs as did Systems and Planning. Buy the whole list (all 10 of them), and double up on the cheaper issues if you wish. I show the list as 100 shares each to make it easier for me to compute the average. Many of these issues will be performing well during late 1983 and 1984—as the big defense contracts come through. So frankly, I'm almost surprised that many of them are doing as well as they are now. But defense is going to be a big factor in the future—bigger than most people envision now. Unless, of course, the Russians give up on their plans to dominate the world.

		2/25/83 Price	Current Price	
NYSE	Harris Corp. (HRS)	49 1/2	43 7/8	Defense stock average based on 1 share of each this week is 269
NYSE	LFE (LFE)	11 7/8	14 1/4	
NYSE	Planning Research (PLN)	14 3/8	17 1/8	
NYSE	Scientific Atlanta (SFA)	19	15 3/4	
NYSE	Tracor (TRR)	28 3/4	34 1/4	
AMEX	Bolt Beranek (BBN)	37	43 1/8	
AMEX	BDM (BDM)	43 1/2	62 1/4	
AMEX	Dynalectron (DYN)	12 3/4	12 5/8	
AMEX	Moog B (MOGB)	15 1/2	17 5/8	
AMEX	Systems Planning (SPZ)	7	8 3/8	
	Original purchase date Feb. 25 '83		239	

GOLD: This gold chart is from the report put out by my good friend, Harry Browne. The mathematics of the gold action since 1980 is worth studying. The bear market which started from the 1980 peak of 850 took gold down to a low of 296. A halfway recovery back to the high would have entailed a gold advance to 573. But so far, the highest gold has rallied to is the 511.50 London fix of February 15. Thus gold failed to recover even half of the points lost during the bear market.

At that time I pointed out that everybody and his brother had noted and was talking about "the big head-and-shoulders bottom" in gold. That the pattern was there was undeniable. That everybody saw the pattern was not a good sign.

Gold broke out of the head-and-shoulders bottom, pushed up to 511.50, then dove down to a low (February 28) of 408.50. The right shoulder of the widely-advertised head-and-shoulders bottom had collapsed. Gold bulls were in shock. But the break was explained away as a freak, a mistake, or perhaps just too many people waiting for the head-and-shoulders breakout.

The loss on the 1983 break was 103 points. A halfway recovery of that break would entail a gold rally to 460. This could indeed occur, but so far the best gold has been able to do is an advance to the 430 area.

I now believe that the 460 area for gold is critical. If gold can better 460, it will have a shot at attacking

the previous 511 high. Bettering 511, I would certainly have to revise my current negative opinion about gold and suggest buying the metal again.

But look at it this way. The money supply has exploded. Ordinarily this calls for inflation 6 months to a year away. And everybody knows this. But gold has, so far, failed to recover even half of its February losses.

In my years of studying market action, I have always placed a good deal of importance on what a tradeable item does at the halfway level of the previous major advance or decline. I will be skeptical (bearish) on gold as long as it fails to better the 460 mark.

I would rather be a buyer of gold at 465 or 515 than I would here. Gold may be at bargain levels, inflation may be about to roar. But there's something amiss in the gold price action. Since 1980 it has failed in a major way to recover even half of its 1980-82 losses. And in 1983 gold has (so far) failed to recoup half of its February losses. Yet, in the face of this, everyone seems positive and bullish on gold. It's food for thought.

From another standpoint, the New York Times (April 11) announced a gold boom coming out of Russia. A new study by Prof. Michael Kaser of Oxford University states that Soviet gold output (which is now around 350 tons a year) will climb to 460 tons by 1990. S. African output has fallen from a peak of 1000 tons in 1970 to 658 tons in 1981. If the Russian-S. African trends continue, by 1990 Russia will be the world's leading gold producer.

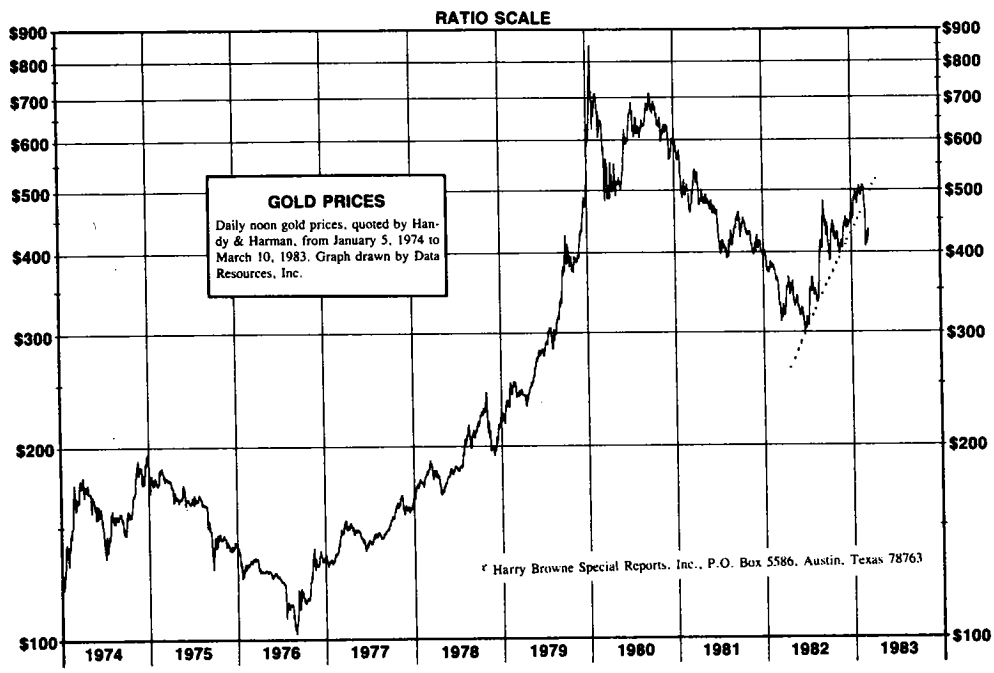
As an aside, Russia is now the world's leading oil producer (12 million barrels per day), Russia is also the world's leading platinum producer. By 1984 Russia hopes to produce 600 billion cubic meters of natural gas, which will roughly equal the US output. Russian coal output to over 1000 million tons by 1990, or about current US output.

So what's my final conclusion on gold? First, I feel gold is rather uninteresting in today's situation. The real action is in the stock market, and my gold-to-common stock ratio is at a multi-year low in favor of common stocks. Second, I'm not at all convinced that the major trend of gold is up. Third, core (survival) positions in gold are warranted, but that's a far cry from holding a major portion of one's assets in gold or gold shares. Finally, it bothers me that almost every hard-money analyst in the nation is bullish on gold. Can they all be right?

	Dow	PTI	Gold
Current	1171	1577	436
5-wk MA	1137		427
13-wk MA	1111		438
50-wk MA	1007		426
3-wk MA		1550	
8-wk MA		1534	
21-wk MA		1482	

LATE NOTES: It's hard to fault this bull market–unless you want to press the point that it's "over-bought." And it is over-bought, but a primary bull market can stay over-bought for weeks and even months on end. The PTI came down and tested its rising trendline–then rallied to new record highs. When I see a market like this I often reverse the situation and pretend I'm on the other side. How would I feel if I were short in this market? I'd feel impecunious–battered and very, very broke. It's as simple as that.

I attach a good deal of importance to the new short interest figures due to come out this week. If the NYSE short interest is up–then this market will probably just continue to climb.



NEXT MAILING : May 4